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The Current and Future Climate of Airline Consolidation: The Possible Impact of an Alliance of Two Large Airlines and an Examination of the Proposed American Airlines-British Airways Alliance

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THE CURRENT AND FUTURE CLIMATE OF AIRLINE CONSOLIDATION: THE POSSIBLE IMPACT OF AN ALLIANCE OF TWO LARGE AIRLINES AND AN EXAMINATION OF THE PROPOSED AMERICAN AIRLINES-BRITISH AIRWAYS ALLIANCE

JEFF MOSTELLER

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I. INTRODUCTION

THIS COMMENT explores the possibility that the alliance between two large airlines will trigger a consolidation within the airline industry. Given the current positive financial state of the airline industry, coupled with a lack of opportunity for sizable expansion of profits, the current climate of the airline industry is one that may view consolidation as possibly the only way to expand airline profit. This Comment argues that the alliance of two large airlines will trigger such consolidation.

It appears likely that such an alliance would create formidable competition in an already ultra-competitive industry and that the remaining airlines will scramble to forge their own alliances with other airlines in order to stay viable in the new market that would follow. This Comment demonstrates that airlines have been preparing for such a possibility for the past few years. Airlines are only waiting on proposed alliances to go through before moving to consolidation as a way of keeping themselves economically viable with this new “mega-airline.”

First, this Comment gives a brief historical overview of airline regulation and the subsequent mergers that followed deregulation. It explores the flurry of consolidation that followed the industry’s 1978 deregulation and the subsequent financial problems that the airlines faced in the wake of those combinations, as well as the relative stability that has occurred in the past few years. Next, this Comment analyzes the current climate of the airline industry with regard to consolidation. It argues that the present environment of the airline industry makes consolidation likely and will examine in some detail the proposed alliance that may serve as the catalyst for an industry-wide consolidation.

This Comment then explores the possible reaction that an alliance between two large airlines might provoke in the airline

industry. It explores the probability that other airlines may follow suit by consolidating. Then, the possible impact that such a consolidation may have on the airline industry, its employees, and airline consumers is examined. It is possible that such an alliance and the subsequent industry consolidation could have both positive and negative effects on all constituencies. Finally, this Comment concludes with an analysis and evaluation of these effects.

II. THE HISTORY OF AIRLINE REGULATION AND CONSOLIDATION

A. BEFORE 1978

In 1938, Congress made the airlines subject to regulation by the creation of the Civil Aeronautics Board (CAB).¹ Congress intended to protect the young industry from excessive competition while also maintaining a certain level of rivalry to promote efficiency.² Congress chose to regulate the young industry after noting the pre-regulation rise of barons in the railroad industry.³ Regulation of the airline industry was designed "to avoid the deleterious consequences of cutthroat and excessive competition, and thereby enhance economic stability, safety, and the sound growth and development of this young industry."⁴

The CAB oversaw airline fares, determined route structures, and regulated several other key industry features.⁵ Under the CAB's regulation, the airline industry had a somewhat "protectionist arrangement."⁶ The CAB disfavored the demise of a major airline or the creation of a new airline.⁷ The CAB promoted this policy by "handicapping" the competition: it expected airlines to use some of their profits from lucrative routes to subsidize marginal routes⁸ while providing weaker airlines with enough routes to keep them from failing.⁹ This practice proved

¹ Civil Aeronautics Act of 1938, 49 U.S.C. app. §§ 401-722 (repealed 1958).

² See Hon. Richard D. Cudahy, *The FERC's Policy on Electric Mergers: A Bit of Perspective*, 18 ENERGY L.J. 113, 125 (1997).

³ See Paul Stephen Dempsey, *Transportation Deregulation—On a Collision Course?*, 13 TRANSP. L.J. 329, 331 (1984).

⁴ *Id.* at 335.

⁵ See Cudahy, *supra* note 2, at 125.

⁶ *Id.*

⁷ See *id.*

⁸ See Paul Stephen Dempsey, *The Dark Side of Deregulation: Its Impact on Small Communities*, 39 ADMIN. L. REV. 445, 457-58 (1987).

⁹ See *To Regulate or Deregulate: An Article of Faith or Analysis?*, 55 ANTITRUST L.J. 205, 206-07 (1986) (panel discussion).

effective for promoting the policy as almost all major airlines survived the regulation period, and no new airlines were created.¹⁰

B. AFTER DEREGULATION: 1978-1989

The airline industry remained under this regulatory scheme for forty years. This changed in the late 1970s when President Carter appointed economist Alfred Kahn as Chairman of the CAB.¹¹ Kahn pushed to diminish entry barriers for new airlines and encouraged price competition among airlines.¹² Dissatisfaction with the CAB's regulation of the airlines culminated in 1978 when Congress passed the Airline Deregulation Act of 1978.¹³ The Act disbanded the CAB and gave its authority to review airline mergers and alliances to the Department of Transportation (DOT).¹⁴ However, the DOT's authority ended on January 1, 1989, when the airline industry, along with all other industries, became subject to the review of the Department of Justice's (DOJ) Antitrust Division.¹⁵

After deregulation, airline consolidation skyrocketed. During the 1980s, the airline industry experienced massive consolidation and growth.¹⁶ In the period between 1978 and 1988 alone, there were fifty-one airline mergers and acquisitions.¹⁷ Some of these mergers were huge such as Frontier and People Express joining Continental, Western merging into Delta, Northwest taking over Hughes Airwest and Republic, TWA acquiring Ozark, and USAir acquiring Piedmont.¹⁸

However, deregulation also brought financial hardship for airlines and service problems for airline consumers. Airline ser-

¹⁰ See Robert M. Hardaway, *Transportation Deregulation (1976-1984): Turning the Tide*, 14 TRANSP. L.J. 101, 134-35 (1985).

¹¹ See Dempsey, *supra* note 3, at 339.

¹² See *id.*

¹³ 49 U.S.C. § 1551(a)(7) (1958) (repealed 1994).

¹⁴ See *id.*

¹⁵ See *id.*; see also Donald T. Bliss & Jacob M. Lewis, *Overseeing Competition in the Airline Industry: Will the Transfer to Justice Make a Difference?*, 34 FED. B. NEWS & J. 293, 293 (Sept. 1987) (exploring the difference in airline merger philosophy between the DOT and the DOJ).

¹⁶ See Michael B. Cox, *Airline Industry Restructuring: From Stuck in the Mud to Flying High*, 16-JUN AM. BANKR. INST. J. 24, 24 (1997).

¹⁷ See Barry E. Hawk, *Airline Deregulation After Ten Years: The Need for Vigorous Antitrust Enforcement and Intergovernmental Agreements*, 34 ANTITRUST BULL. 267, 276 (1989).

¹⁸ See GEORGE WILLIAMS, *THE AIRLINE INDUSTRY AND THE IMPACT OF DEREGULATION* 42 (1993).

vice to smaller communities declined significantly as 260 cities lost air service in the first year after deregulation and forty percent of the nation's airports lost service within two years of deregulation.¹⁹ In 1980, with deregulation having been in effect for only two years, the airline industry suffered record losses of \$280 million.²⁰ By 1982, worldwide airline industry losses were \$900 million despite the additional seven million passengers it had acquired since 1981.²¹

Despite this negative financial climate, many airlines consummated mergers during the decade following deregulation. Several of these airlines later found this strategy to be an unwise choice. Many of the acquiring airlines were soon "hobbled with excessive debt that became more crushing when the economy soured, or found it a nightmare trying to merge the different airlines' labor contracts and employee work rules."²² For example, Pan American World Airways struggled for several years after its 1979 acquisition of National Airlines.²³ Northwest Airlines suffered the same dilemma after buying Republic in 1986.²⁴ Texas Air Corp. eventually collapsed after merging Eastern, People Express, and Continental.²⁵ USAir is one of the few merged airlines that has survived into the present, but it is plagued with high operating costs and is considered among the weakest of the large carriers.²⁶ Regardless of these failures, airline mergers continued to flourish throughout the 1980s.

C. THE 1990s

The expansion trend prevalent throughout the 1980s saw the beginning of its demise on August 2, 1990. Following Iraq's invasion of Kuwait, fuel prices jumped from an average fifty-five cents per gallon to more than one dollar per gallon.²⁷ Within months of this "watershed date," Continental, Pan Am, America West, Midway, and several smaller airlines filed for bankruptcy.²⁸

¹⁹ See Dempsey, *supra* note 3, at 359; see also Dempsey, *supra* note 8, at 455.

²⁰ See Dempsey, *supra* note 3, at 342.

²¹ See *id.*

²² James F. Peltz, *Airline Mergers '90s-Style Might Stand a Better Chance This Time*, L.A. TIMES, Dec. 5, 1996, at D1, available in 1996 WL 12762903.

²³ See *id.*

²⁴ See *id.*

²⁵ See *id.*

²⁶ See *id.*

²⁷ See Cox, *supra* note 16.

²⁸ See *id.*

In addition, Pan Am, Midway, and Eastern Airlines ultimately liquidated their assets.²⁹

Since this earlier part of the decade, however, the airline industry has enjoyed a period of relative calm. When comparing the airline industry of the 1990s with that of the 1980s, the 1990s have been relatively stable in terms of airline mergers and acquisitions.³⁰ There have not been the large mergers and subsequent bankruptcies that characterized the 1980s for several years.³¹ In fact, the main airline event over the past few years has been the continued battle between larger, established carriers and low cost, low-fare start up carriers.³² While there have been a handful of merger proposals and discussions in the past few years, they have typically been with the smaller, low-fare carriers and have not had a large effect on the industry. Recent examples include 1997's ValueJet-AirWays merger and the Western Pacific-Frontier merger.³³

In 1995 this stability appeared to be in danger when USAir initiated talks with United Airlines and American Airlines.³⁴ Those talks eventually broke down due to USAir's high labor costs.³⁵ However, the possibility of a USAir alliance was enough to rekindle the airline industry's attention on consolidation.³⁶ This attention to the possibility of industry-wide consolidation is now prevalent.

III. THE PRESENT PRO-CONSOLIDATION ENVIRONMENT

The current climate of the airline industry is conducive to consolidation in the near future. Every airline appears to be preparing itself for the next big airline alliance. As one airline analyst has noted, even if most airline executives are not eager to consolidate, they do not want to be unprepared if their competitors start allying themselves: "I think the flurry of talks

²⁹ See *id.*

³⁰ See Richard Tomkins, *US Airlines Locked on to a Consolidation Flight-Path*, FIN. TIMES, Dec. 6, 1996, at 29, available in 1996 WL 13953591.

³¹ See *id.*

³² See *id.*

³³ See Steve Huettel, *ValueJet Targets New Image, Routes With AirTran Merger*, TAMPA TRIBUNE, July 11, 1997, at 1, available in 1997 WL 10796840; see also Penny Parker, *Low-fare Air Merger Takes Flight WestPac and Frontier Forming New Company*, DENV. POST, July 1, 1997, at A01, available in 1997 WL 6078147.

³⁴ See Tomkins, *supra* note 30.

³⁵ See *id.*

³⁶ See *id.*

around USAir . . . caused all of the companies to look at that [merger] possibility and think of the various scenarios that may unfold They may have various contingency plans in their vaults. It is a topic that is waiting on the back burner.”³⁷

A. THE CURRENT PRO-CONSOLIDATION CLIMATE

In 1996, the airlines generated record profits while also enjoying strong stock prices.³⁸ Despite such profits, growth prospects for airlines are few as the industry has matured. Many analysts consider airline consolidation to be the “natural next step” as it has been in the defense, railroad, and trucking industries.³⁹ Airlines have tried improving their growth by adding more hubs to their networks and adding international alliances, but they are only enjoying around three percent annual domestic growth.⁴⁰ This and the over-capacity and huge losses of the early 1990s seems to have taught the airlines that expanding capacity will not allow them to grow domestically.⁴¹ The new philosophy is that the economy can only support the approximately 4000 airplanes already being utilized, and the only way to increase ridership is by reducing fares and enduring losses.⁴² Thus, the new airline thinking may be that it is “[b]etter to buy a competitor than [it is] to bury one by adding airplanes, cutting fares and stealing passengers.”⁴³ Some believe that “[t]he theory that it is cheaper and easier to do the growth internally is now seen as a fallacy.”⁴⁴

Therefore, airline consolidation may be viewed by many as the only way to increase an airline’s growth. The acceptance of

³⁷ *Top 1997 Issues are Earnings, Alliances, Safety and FAA Funding*, AIRLINE FIN. NEWS, Jan. 6, 1997, available in 1997 WL 7878983 (quoting Phil Bagley, a debt analyst with Standard & Poor) [hereinafter *Top 1997 Issues*]. A more recent assessment has stated that “[a]irline alliances are all the rage.” Michael Miller, *The Last Word: Airlines Jump on the Alliance Bandwagon*, AIRLINE FIN. NEWS, Nov. 9, 1998, available in 1998 WL 7198091 (reporting a June 1998 survey that there are 502 non-regional airline alliances worldwide, a 38 percent increase from 1997).

³⁸ See Scott McCartney & Martha Brannigan, *High Anxiety: Behind Talks of Delta, Continental Are Fears of Being Left Behind*, WALL ST. J., Dec. 5, 1996, at A1, available in 1996 WL-WSJ 11808502.

³⁹ See *Behind Delta-2: A New Round of “Monopoly”?*, DOW JONES NEWS SERV. (Dec. 4, 1996) [hereinafter *Behind Delta*].

⁴⁰ See *id.*

⁴¹ See Scott McCartney, *Consolidation May Be Only Way for Airlines to Grow*, WALL ST. J., Nov. 20, 1995, at B5, available in 1995 WL-WSJ 9908696.

⁴² See *id.*

⁴³ *Id.*

⁴⁴ *Id.* (quoting Thomas Longman, a Lehman Brothers analyst).

consolidation as a viable option for the airline industry has been offered by analysts for at least a couple of years now. As one analyst stated in 1996, "[a]s the industry matures, consolidation is the way to eke out the last bit of growth It's looming out there, especially when you have a catalyst."⁴⁵ The rationale behind this theory is that as industries consolidate, their profit margins will stabilize or rise, and the stock's price-earnings multiples will also rise.⁴⁶ In 1995, another industry analyst was quoted as labeling consolidation as "the only way to go" for airlines in 1996 and noted that the problem major airlines would face in 1996 would be what "to do for an encore after one of the most stunning turnarounds in the history of the business."⁴⁷ A more recent assessment predicts that "the next three years are likely to be quite interesting as airlines take advantage of existing alliances to go to the next step and merge."⁴⁸

Some airline executives appear to be in agreement with this assessment. John Harper, USAir's chief financial officer, predicted in late 1995 that there would soon be "another consolidation phase in this industry. You can't have us middle-tier carriers on a long-term basis."⁴⁹ Another airline executive stated support for industry consolidation: "I've always seen a reason for consolidation. And I don't think it's too soon."⁵⁰

Thus, since at least 1995 there seems to be a general attitude in the airline industry that consolidation is inevitable. The current economic climate of the airline industry seems to continue to support this attitude that the airline industry is ripe for consolidation.

1. *The Economic Climate*

The airline industry is still a mature industry with robust earnings and excess cash, but with few opportunities for internal investment.⁵¹ There is still over-capacity in the industry and thus

⁴⁵ *Behind Delta*, *supra* note 39 (quoting Kevin Murphy, a Morgan Stanley analyst).

⁴⁶ *See id.*

⁴⁷ McCartney, *supra* note 38 (quoting Thomas Longman, a Lehman Brothers analyst).

⁴⁸ *Open Skies Will Be Needed to Allow Wave of Mergers*, AIRLINE FIN. NEWS, Mar. 31, 1997, available in 1997 WL 7879087 [hereinafter *Open Skies*].

⁴⁹ McCartney, *supra* note 41.

⁵⁰ *Id.* (quoting an unidentified airline CEO).

⁵¹ *See id.*

"consolidation talks may accelerate now, not decelerate . . . [as these] are ideal conditions for these types of deals."⁵²

It also appears that the current economic environment of the airline industry provides airline consolidation with a greater chance of success than past attempts. Most major airlines today operate with lower costs than they did in the 1980s.⁵³ In addition, airlines have been enjoying a healthy economy and strong passenger traffic which have produced enormous profits.⁵⁴ It also appears that airlines are "wisely using their current, swollen earnings to pay down their debts and have only cautiously ordered new aircraft so as not to fly too many empty, expensive seats" and have "for now, laid off their old habit of constantly slashing fares, a tactic that protected their market shares but wreaked havoc with their profits and helped saddle them with more than \$10 billion of losses between 1990 and 1994."⁵⁵

2. *Non-Economic Reasons*

There also appear to be non-economic reasons for believing that airline consolidations will be more successful now than in the past (and, thus, more likely to happen). The negative experiences that many airlines endured in the past may have taught airline executives what to avoid. As one industry analyst has stated, "There's a greater chance. . . [of success] if only because everyone knows what flops the previous mergers had been."⁵⁶ Another non-economic element may have changed which could improve merger success - the egos of airline executives.⁵⁷ In the past, airline executives seemed to thrive on making their airline the biggest regardless of cost, assuming that size would enable their airline to push out smaller airlines.⁵⁸ Today, airline executives appear more concerned with a profit.⁵⁹ Continental Chairman Gordon Bethune has supported this theory pointing out that "what counts today in the airline business is not size, but making money."⁶⁰ Many believe that with the cur-

⁵² *Id.* (quoting Vivian Lee, an analyst with BT Securities, a unit of Bankers Trust).

⁵³ See Peltz, *supra* note 22.

⁵⁴ See *id.* (predicting combined airline profits to hit a record \$2.5 billion or more for 1996).

⁵⁵ *Id.*

⁵⁶ *Id.* (quoting Jeffrey Long, an analyst for J.P. Morgan Securities Inc).

⁵⁷ See *id.*

⁵⁸ See *id.*

⁵⁹ See *id.*

⁶⁰ *Id.*

rent financial state of the airline industry, the best way of making money would be further consolidation through mergers of major airlines.⁶¹ With major airlines putting global networks in place in order to compete on a worldwide basis, which would mean greater profits, "stronger market strength on the home-front. . . would only cement in place a truly global network."⁶²

3. *The Alternate Catalyst: Stock Prices*

Before continuing, there is one consolidation catalyst that should at least be briefly considered. While this Comment focuses primarily on the possibility of airline consolidation following the alliance of two large airlines, outside economic forces could effectuate the same result. At least one analyst has speculated that a significant drop in stock prices could spark airline consolidation.⁶³ These reduced stock prices would lower the cost of acquiring an airline.⁶⁴ This possibility is unattractive to smaller airlines that might not be desirable enough to attract an acquirer, making some of them unable to survive such a scenario.⁶⁵ However, as likely as this scenario may be, it appears even more likely that an alliance of two large carriers will be the impetus that drives other airlines to consolidate. Therefore, the alliance that appears most likely to trigger such an airline industry consolidation will now be examined.

B. THE PROBABLE CONSOLIDATION CATALYST: THE PROPOSED AMERICAN AIRLINES-BRITISH AIRWAYS ALLIANCE

This Comment will now analyze the recent merger possibility that has drawn the greatest speculation as being the final impetus for industry-wide consolidation. As has been previously asserted, if airline consolidation does occur, it will likely be sparked by the alliance of two large airlines. The ongoing proposed alliance between American Airlines and British Airways has continually been identified as the most likely candidate for this catalyst. Their talks have already made other airlines consider the possibility of consolidation. For example, Gordon Bethune, Continental's CEO, told employees after the

⁶¹ See *Future of Airline Mergers May Extend to U.S. Major Carriers*, WORLD AIRLINE NEWS, June 6, 1997, available in 1997 WL 8541724 [hereinafter *Future*].

⁶² *Id.* (quoting Susan Donofrio, an analyst with NatWest Securities).

⁶³ See *Top 1997 Issues*, *supra* note 37 (quoting Dave Trietal, president of the New York based aviation consulting firm, SH&E).

⁶⁴ See *id.*

⁶⁵ See *id.*

announcement of the British Airways-American Airlines talks that such an alliance could lead to industry consolidation.⁶⁶ The reason for this reactionary response is a matter of staying competitive. An alliance between two large airlines, both of which provide substantial competition to other airlines, would create an even larger competing entity. Many airlines might feel that they would have no choice but to ally themselves in order to survive the heightened competition following such an alliance. This could have a domino effect, forcing other airlines to combine in order to keep up with the other newly-consolidated airlines.

Thus, it is understandable that many airlines (and the airline industry in general) are in the consolidation mindset. It would simply not be sound business judgment to ignore exploring responses to a consolidation scenario given the current forecast that consolidation is probable. Therefore, it is not only understandable but necessary for airline executives to examine potential buyers or sellers of their airlines in order to be prepared if a large alliance does occur. They would then be in a position where their planning may help keep their airline competitive (or even solvent). Indeed, many airline officials are already planning alliances with other airlines in order to compete against these proposed alliances.⁶⁷ Many airline industry analysts are in agreement that an alliance between two larger airlines will cause other airlines to attempt to merge.⁶⁸

1. *The Proposed Alliance*

On June 11, 1996, former rivals American Airlines and British Airways announced their plans for a proposed alliance between the two airline giants.⁶⁹ The proposed alliance remains uncompleted. However, it is likely that this alliance, if successful, will be the final catalyst that drives the airline industry to consolidate.

The alliance, as originally proposed, would have involved both airlines pooling costs and revenues, planning strategies such as route structuring and fares, feeding passengers to each

⁶⁶ See *id.*

⁶⁷ See *id.*

⁶⁸ See *id.*

⁶⁹ See AMR Corp. Communications, *American Sees Progress by Regulators in British Airways Alliance Review* (visited Nov. 2, 1997) <<http://www.amrcorp.com/amr/sep0897b.htm>> (AMR Corp.'s official website for American Airlines. AMR Corp. is American Airlines' parent company) [hereinafter AMR Corp., *Progress*].

other, and possibly swapping equity stakes of up to twenty percent.⁷⁰ American Airlines stated that the original alliance proposal had three main elements:

1. Coordination of all passenger and cargo services that the two carriers operate between the United States and Europe, with profit sharing on Alliance services.
2. Codesharing across each other's global networks; wherever possible, American will place its "AA" designator code on British Airways' transatlantic services and flights beyond BA's European gateways, and British Airways will place its "BA" code on American's transatlantic services and flights beyond American's U.S. gateways.
3. Establishment of a fully reciprocal, worldwide frequent flyer program.⁷¹

It appears that the impetus behind the AA-BA alliance is the recognition of the need to stay competitive in an increasingly global market. At least from American Airline's view, it is this same recognition that sparked the other major global airline alliances of recent years such as the Luftansa-United-SAS, KLM-Northwest, and Delta-Sabena-Swissair-Austrian alliances.⁷² According to American Airlines:

The airline industry is a network business. In the past, carriers built linear route systems, and were content to transfer passengers to another airline to get them to their destinations. Follow-

⁷⁰ See *British Airways, AMR Mull Possible Alliance*, WEST'S LEGAL NEWS, June 3, 1996, available in 1996 WL 288746 [hereinafter *BA, AMR Mull*]. However, this more ambitious alliance has been put on hold. Due to the continuing regulatory hurdles discussed later, both airlines have offered to phase the alliance in over four to five years if that timetable would make it more acceptable to regulators. See Terry Maxon, *British Air, American Redo Alliance Plans*, DALLAS MORNING NEWS, Oct. 31, 1998, at 1F, available in 1998 WL 13114964; see also *infra* notes 75-82 and 89-95 and accompanying text (discussing specific regulatory hurdles that provoked the announcement of a scaled back alliance). The airlines now plan to codeshare in the U.S. domestic and European Union markets (which is argued as allowable under the existing Bermuda II bilateral) but delay other co-operation such as price coordination, revenue sharing, capacity, and schedule planning until regulatory approval is granted. See Tom Gill, *BA/American Put Alliance Brakes On*, AIRLINE BUS., Dec. 1, 1998, available in 1998 WL 11817520. In addition, falling yields of 4.3% on first class and business passengers were cited as a further reason for postponement of the original alliance plan. See *id.*

⁷¹ AMR Corp. Communications, *The American Airlines-British Airways Alliance Will Benefit Consumers and Enhance Competition* (visited Nov. 2, 1997) <<http://www.amrcorp.com/amr/oct1496a.htm>> [hereinafter *AMR Corp., Benefit*].

⁷² See *id.*; see also *Rivals Attack British-American Airline Deal: Lines Fear Price Gouging by Alliance*, COURIER J. (Louisville, Ky.), June 12, 1996, at 8B, available in 1996 WL 6350078 [hereinafter *Rivals*].

ing deregulation of the domestic U.S. airline industry in 1978, airlines abandoned linear route systems in favor of hub-and-spoke networks, which greatly increased efficiency and geographical scope. In the past few years, this process has begun to take root in international aviation. International air carriers now recognize that global hubs are an effective way to keep customers on their network or that of a partner, and that hub-and-spoke networks provide more choice and convenience to passengers and shippers, and more benefit to the airline.⁷³

2. *Obstacles to the Alliance*

Perhaps because of the widespread consequences involved with this alliance, it has been examined carefully by all involved and, as discussed previously, several factors have caused its full implementation to continue to be delayed. Regulatory considerations by both the United States and British governments have halted the completion of the alliance. However, it is believed that the U.S. and U.K. governments will eventually approve the alliance.⁷⁴ In addition, resistance by rival airlines arguing potential antitrust violations and other factors have caused the alliance to continue to languish as a proposal.

a. The Passage of an "Open Skies" Pact

One of the major hurdles facing the AA-BA alliance is the passage of an open skies pact between the United States and Britain. The U.S. government has declared that it will not approve the alliance unless Britain agrees to an open skies pact. The United States has similar agreements with a dozen countries, including Germany, as well as "liberalized" air transportation pacts with nearly thirty other countries.⁷⁵ Bill Schulz, a spokesman for the DOT indicated that this policy was intended "to ease restrictions on rival carriers, which could be crippled by such a transportation titan."⁷⁶ According to Mr. Schulz, the U.S. government has "made it clear to the British that an open-skies agreement ensuring free competition would be a prerequisite for consideration of antitrust immunity for such an alliance."⁷⁷ An open skies treaty would provide British and U.S. air carriers

⁷³ AMR Corp., *Benefit*, *supra* note 71.

⁷⁴ See *Top 1997 Issues*, *supra* note 37.

⁷⁵ See Laura Myers, *2 Airlines Seek Permission For Alliance*, DENV. POST, Jan. 11, 1997, at D08, available in 1997 WL 6061956.

⁷⁶ *Id.*

⁷⁷ *Id.*

unrestricted access to airport hubs.⁷⁸ Both airlines have stated that they agree with such a policy, advocating that their proposed alliance promotes open competition, and lower ticket prices.⁷⁹

The regulatory hurdle has been a continuing impediment to the proposed alliance. Both airlines originally projected that they would be granted regulatory clearance by November of 1996.⁸⁰ However, this goal was not met. Indeed, almost a year later, with the open skies agreement *still* not having been completed, U.S. Transportation Secretary Rodney Slater projected that the agreement would be sealed by the end of 1997.⁸¹ However, even at the time of Secretary Slater's comments, there were still no set dates for a resumption of aviation talks with Britain. In addition, the DOT announced plans to hold hearings on the pact that would follow a two-month comment period, making it unlikely to obtain approval by the end of 1997. Secretary Slater, perhaps acknowledging the considerable time delays that the pact's passage had already caused stated further, "I know it's optimistic but I think we can get closure by the end of the year."⁸² This assessment was indeed optimistic as the U.S. and U.K. governments have still not solidified the open skies agreement and it does not appear that they will any time in the foreseeable future. Thus, if for no other reasons, the original American Airlines-British Airways alliance may not be successful because of the enormous difficulties involved in getting one government (let alone two) to finally agree on the open skies agreement.

b. Antitrust Concerns

Closely tied to the issue of an open skies agreement is the argument raised by rival airlines that the American Airlines-British Airways alliance would stifle competition from other airlines. Presently, American Airlines and British Airways carry around

⁷⁸ See BA, *AMR Mull*, *supra* note 70.

⁷⁹ See Myers, *supra* note 75.

⁸⁰ See CNN Travel News, *Months Late and No Signs of Progress for British Airways-American Deal*, Aug. 20, 1997 (visited Nov. 2, 1997) <<http://cnn.com/TRAVEL/NEWS/9708/20/air.alliance.ap/>>.

⁸¹ See CNN Travel News, *U.S. Transportation Secretary Says Open Skies Deal Coming Soon*, Sept. 8, 1997 (visited Nov. 2, 1997) <<http://cnn.com/TRAVEL/NEWS/9709/08/air.update.reut/>>.

⁸² *Id.* Over a year after *this* comment, U.S. negotiators prematurely ended talks with British officials stating Britain "was not prepared to resolve any of the core issues," and a few days later, the U.S. Department of Transportation postponed hearings on the alliance indefinitely. See Terry Maxon, *supra* note 70.

sixty percent of the airline traffic between the United States and Britain.⁸³ If the alliance is approved, they would no longer compete against one another. Many airlines have warned that the alliance would become nothing more than a "massive transatlantic price-gouging cartel" since they would control sixty percent of the U.S.-U.K. market.⁸⁴ Continental president and CEO, Gordon Bethune has argued that "[t]he two largest trans-Atlantic carriers should not be allowed to combine their operations without requiring a substantial divestiture of assets to assure genuine competition."⁸⁵ One of the more scathing criticisms came from Virgin Atlantic Airways (British Airways' arch rival) chief Richard Branson, who accused American Airlines and British Airways of setting "a new world's record for chutzpah by proposing what has come to be called the 'merger from hell.'"⁸⁶ American Airlines has dismissed the claims that the alliance would hamper competition or fix prices. According to Donald Carty, American's president, "If someone comes in and lowers prices and we don't respond, we won't have 60 percent' of the traffic between the United States and Britain."⁸⁷ Likewise, British Airways CEO Bob Ayling has responded that the alliance would increase competition and lower fares.⁸⁸

c. Heathrow Airport and the European Commission

One of the crucial elements connected with the proposed alliance is airline access to the coveted takeoff and landing slots at London's Heathrow airport. Britain presently only allows two U.S. airlines, American and United, to fly into Heathrow.⁸⁹ The U.S. government has insisted that Heathrow be opened to other airlines before approving the British Airways-American Airlines

⁸³ See *Rivals*, *supra* note 72.

⁸⁴ Dirk Beveridge, *Plan By United Rivals Still In Holding Pattern*, DENV. POST, Aug. 20, 1997, at C03, available in 1997 WL 6082631.

⁸⁵ *Rivals*, *supra* note 72. TWA Chairman Gerald Gitner sent a letter to President Clinton stating trans-Atlantic alliances such as the American Airlines-British Airways alliance hamper his company's ability to compete fairly and that exempting such alliances from antitrust regulation would allow such carriers "to fix prices and travel agent commissions as well as divert traffic from competing carriers." Kyung M. Sony, *Airline Alliances are Unfair to Competitors*, TWA Chairman Says, KNIGHT-RIDDER TRIB. BUS. NEWS, Dec. 9, 1998, available in 1998 WL 16352859.

⁸⁶ Beveridge, *supra* note 84.

⁸⁷ *Rivals*, *supra* note 72.

⁸⁸ See *id.*

⁸⁹ See Beveridge, *supra* note 84.

alliance.⁹⁰ The aforementioned open skies agreement would allow other U.S. airlines such as Delta, Northwest, Continental and TWA to also provide service to Heathrow.⁹¹ American Airlines has claimed that the alliance would result in more competition by giving more airlines access to Heathrow.⁹²

In addition to the necessity of satisfying the United States and British governments, the proposed alliance also has to meet with the approval of the European Commission (EC). The EC has long stated that it will block the alliance if the airlines do not make concessions on slots at Heathrow.⁹³ As a commission spokesman has warned, "If they don't give any commitments on slots, there should be no surprise that we could not accept such an alliance."⁹⁴ The EC informed American Airlines and British Airways in July of 1997 that they would have to make room for other airlines by giving up 350 slots, most at the congested Heathrow airport.⁹⁵

d. Rival Airlines' Concerns and American's Response

Despite assurances to make slots available and the claims of American Airlines and British Airways, numerous airlines and other organizations have taken a skeptical view of the proposed alliance. The United States Senate has held hearings on the

⁹⁰ See *id.*

⁹¹ See *Rivals*, *supra* note 72.

⁹² See AMR Corp., *Progress*, *supra* note 69 (quoting Arnold Grossman, American Airlines' Vice President of International Affairs). There may be some merit to this argument. Some analysts have speculated that the only way London airports will be opened up for other airlines is if the alliance goes forward. See, e.g., Terry Maxon, *Airline Alliance Progresses: European Regulators Outline Restrictions on British Airways-American Proposal*, DALLAS MORNING NEWS, July 9, 1998, at 1D, available in 1998 WL 13086433 (quoting Sam Buttrick, an analyst with Paine Webber Inc.).

⁹³ See Amelia Torres, *EU Reiterates Hurdle to BA, AA Airlines Deal* (visited Nov. 7, 1997) <<http://www.infoseek.com/Content?arn=A1608...oframes&col=Nx&svx=LHsnx&ak=NEws1486&kt=A>> (Infoseek: The News Channel webpage reporting a Nov. 5, 1997 Reuters news service story).

⁹⁴ *Id.* For an in-depth analysis of the EC's review of the alliance, see G. Porter Elliot, *Learning to Fly: The European Commission Enters Unfamiliar Skies in its Review of the British Airways-American Airlines Alliance*, 64 J. AIR L. & COM. 157 (1998).

⁹⁵ See Torres, *supra* note 93. One year later, this was revised to 267 specific slots. See also Michael Skapinker & Samer Iskandar, *EU Riders to BA-American Pact Approval*, FIN. TIMES, July 31, 1998, at 4, available in 1998 WL 12255915. This obstacle has proven to be a formidable one as it caused British Airways to forgo immediate approval and instead settle for a scaled back plan of alliance. See Laurence Zuckerman, *British Airways Seeking Phased-in Link With American*, N.Y. TIMES-ABSTRACTS, Oct. 31, 1998, at C2, available in 1998 WL 22330602; see also *supra* note 70.

proposed alliance.⁹⁶ Senator Mike Dewine (R-OH), Chairman of the Senate Antitrust, Business Rights, and Competition Subcommittee, which held one such hearing on the American-British Airways alliance, stated:

Competition is essential to cost and convenience for the airline travelers. . . . As global transportation expand in the next century, it is important that the marketplace provide all consumers with competitive prices, quality services, and a variety of travel options. Those of us on Capital [sic] Hill want to be certain that the impact of this proposed alliance on competition, air fares for consumers, and the viability of the industry is fully examined.⁹⁷

At the hearing, Barry Simon, Senior Vice President, International of Continental Airlines gave lengthy testimony voicing many airlines' trepidations of the American Airlines-British Airways alliance.⁹⁸

American Airlines, in an official release, responded to what it saw as the three principal arguments being made by most opponents of the alliance: (1) the alliance would be too large, (2) the alliance would dominate U.S.-U.K. air travel and would increase prices, and (3) even with an open skies agreement, genuine competition would be impossible because of the slot and facility constraints at London's Heathrow Airport.⁹⁹ American Airlines responded to each argument in turn. It argued that the American Airlines-British Airways alliance would actually be smaller than two existing alliances: the Lufthansa-United-SAS alliance and the KLM-Northwest Alliance.¹⁰⁰ Next, American disputed the claim that the proposed alliance would dominate the U.S.-

⁹⁶ See Mike Dewine, *Dewine Calls For Hearings on Proposed Airline Merger*, GOV'T PRESS RELEASES, Apr. 14, 1997, available in 1997 WL 4431612.

⁹⁷ *Id.*

⁹⁸ See *The Antitrust Implications of the Proposed British Airways-American Airlines Alliance Before the Antitrust, Business Rights, and Competition Subcomm. of the Senate Comm. on the Judiciary*, 104th Cong. (1997) (statement of Barry P. Simon, Senior Vice President, International for Continental Airlines), available in 1997 WL 10569895. Mr. Simon made numerous proposals and points of criticism involving the proposed alliance. Among them were that: (1) the alliance will be able to fix prices, divide markets, allocate capacity, etc. with complete immunity from antitrust laws, (2) the alliance is anti-competitive, (3) the "open skies trade" proposed by the airlines is not the solution to the anticompetitive effects of the alliance, and (4) the Departments of Transportation and Justice must thoroughly investigate the alliance. See *id.*

⁹⁹ See AMR Corp., *Benefit*, *supra* note 71.

¹⁰⁰ See *id.* American went on to elaborate by comparing its proposed alliance with British Airways (BA) with that of the Lufthansa-United-SAS (LUS) alliance. While it stipulated that the BA alliance would be approximately the same size as

U.K. market by arguing that “[a] forthcoming study of the likely effects of U.S.-U.K. open skies projects that after five years, the combined share of American and British Airways in the U.S.-London market will decline from the 61 percent under today’s restrictions, to 41 percent under open skies, a drop of 20 points.”¹⁰¹ Finally, American argued that Heathrow Airport is not “full” by pointing out that forty-five new airlines have been able to secure slots at Heathrow since 1991 and seventy-one daily peak-hour slots have been added at Heathrow in the four year period between 1992 and 1996.¹⁰²

e. Other Obstacles

In addition to the regulatory hurdles that American Airlines and British Airways must overcome in the passage of an open skies agreement and passing antitrust scrutiny, there are other miscellaneous obstacles being placed in front of the alliance. While some airline executives have been testifying against the alliance or publicly condemning it, others have taken a more aggressive approach.

Some rival airlines have attempted to obstruct the alliance by slowing the review of the European Commission.¹⁰³ Such rivals as United Airlines and Delta have been slow in providing information about their operations to the European Commission.¹⁰⁴ While the airlines denied this charge, analysts have stated that rival airlines would have much to gain by slowing approval of the alliance as it interferes with the coordination of American Air-

LUS in terms of revenue passenger miles, it claimed the BA alliance was smaller in other areas supplying the following measures:

MEASURE	LUS	AMERICAN-BA
Revenue passenger miles	160.4 billion	165.3 billion
Worldwide destinations	472	388
Jet aircraft operated	903	878
Total employees	161,000	137,000

See id.

¹⁰¹ *Id.* American argued that this forty-one percent would be “substantially smaller than the current market shares of other transatlantic alliances at their European gateways.” *Id.*

¹⁰² *See id.*

¹⁰³ *See* Peter Robison, *Ruling on Airline’s Alliance to Be Delayed*, FORT WORTH STAR-TELEGRAM, Feb. 12, 1998, available in 1998 WL 3276345.

¹⁰⁴ *See id.*

lines' and British Airway's schedules.¹⁰⁵ As one analyst has stated, "The longer it's delayed, the longer BA and American Airlines lose market share to the other alliances."¹⁰⁶

In a more litigious approach, USAir brought a lawsuit against the proposed American Airlines-British Airways alliance claiming that; 1) the alliance would breach a 1993 investment agreement that British Airways made with USAir, 2) American Airlines was interfering with the contract, and 3) the alliance would violate antitrust laws.¹⁰⁷ A federal judge eventually dismissed the interference allegation against American Airlines on a technicality, but reserved judgment on the antitrust claims.¹⁰⁸ Lawsuits such as this are just one of the numerous impediments to implementing the alliance.

IV. THE FORECAST FOR AIRLINE INDUSTRY CONSOLIDATION AFTER THE ALLIANCE OF TWO LARGE AIRLINES AND ITS IMPACT

This part begins with the premise that the proposed American Airlines-British Airways alliance is successful. After years of preparation, debate, and legislative maneuvering, the alliance overcame seemingly insurmountable odds and is finally implemented. Would other airlines begin to ally themselves with former rivals and what would be the effects? How would it impact the other airlines that would have to compete with the new American Airlines-British Airways giant? How would industry consolidation affect airline employees? Finally, how would airline industry consolidation affect airline consumers? Each of these questions will now be addressed in turn.

A. EFFECT ON THE AIRLINE INDUSTRY

Would a successful American Airlines-British Airways alliance be the catalyst for industry consolidation? This has been de-

¹⁰⁵ See *id.* Delta, United, Continental, US Airways, Transworld and Tower Air recently urged the U.S. Transportation Department to dismiss the application from American and British Airways. See *Six U.S. Airlines Urged the U.S. Transportation Dept. to Dismiss*, AVIATION WK. AND SPACE TECH., Nov. 16, 1998, at 22 available in 1998 WL 19818960.

¹⁰⁶ *Id.* (quoting Andrew Light, an analyst with Salomon Smith Barney in London).

¹⁰⁷ See Karen Schwartz, *Judge Dismisses Part of USAir Suit Against BA-American Alliance* (visited Nov. 2, 1997) <http://sddt.com/files/librarywire/96wireheadlines/10_96/DN96_10_25/DN96_10_25_fo.html> (SOURCE NEWS & REPORTS webpage reporting an Oct. 25, 1996 Associated Press story).

¹⁰⁸ See *id.*

bated in industry circles since the announcement of the proposed alliance. While some doubt the probability of large scale consolidation, many airline officials have been planning to align themselves with other carriers for years in order to prepare themselves for the unattractive possibility of competing against the AA-BA combination.¹⁰⁹ Industry analysts tend to agree with the consolidation scenario. As one analyst said,

What is clear is that if there is one big merger, there will be several. . . . The potential market and revenue power of a big route network is considered too threatening to be ignored by the regulators at the same time as the first deal. That way, the government would have to consider the full consequences of consolidation before giving the green light to anyone. The assumption is the Department of Transportation will either accept all the deals or none of them, but probably not pick and choose.¹¹⁰

Another analyst predicts that "[if] the [AA-BA] transaction were to go through, we think it would force other carriers to consider strategic alternatives including acquiring another airline."¹¹¹ Yet another analyst predicts both international and domestic airline mergers following an AA-BA alliance because other airlines would be "terrified that BA and American will work something out and have control of about one-fourth of the world market."¹¹²

For all the talk and preparation of consolidation, some analysts and airline officials do not believe that a wave of mergers would follow the alliance. United Chairman Gerald Greenwald has stated that he does not believe one merger would necessarily cause a "chain reaction."¹¹³ One reason given for disbelieving

¹⁰⁹ See *Top 1997 Issues*, *supra* note 37 (quoting Phil Bagley, a debt analyst with Standard & Poor's); see also Charles Boisseau & Bill Mintz, 'Open Skies' May Propel Mergers/Continental's Talks with Delta *Timely*, HOUSTON CHRON., Dec. 5, 1996, at 1, available in 1996 WL 11580001 (quoting Susan Donofrio, an analyst with NatWest Securities speculating that the rationale behind the 1996 proposed Delta-Continental alliance as "it's better to pursue a merger partner of [Continental's] own choosing 'rather than scrambling to find their own later.'").

¹¹⁰ *Top 1997 Issues*, *supra* note 37 (quoting Phil Bagley, a debt analyst with Standard & Poor's).

¹¹¹ David Field, *Airline Merger Wave Shows Up On Radar*, USA TODAY, Dec. 5, 1996, at 3B, available in 1996 WL 2078473 (quoting Candace Browning, an analyst with Merrill Lynch).

¹¹² *Id.* (referencing Barbara Beyer, a consultant with Avmark).

¹¹³ See Boisseau & Mintz, *supra* note 109.

that airline consolidation will occur is "[t]hat there are not enough strong companies to be acquired."¹¹⁴

Antitrust concerns may be another reason that consolidation might not occur. Some airline industry analysts believe that the Clinton Administration's antitrust regulators would simply not allow a wave of mergers that could decrease competition.¹¹⁵ One analyst described this scenario when discussing the 1996 proposed Delta-Continental combination. He speculated that if a Delta-Continental combination sparks other major airlines to merge, then the airline industry will only be left with three or four major carriers that would control eighty-percent of the U.S. airline business, and "that ain't gonna fly."¹¹⁶ However, some analysts argue that a wave of mergers could leave the airline industry with five or six major airlines (instead of nine), but this may not be sufficient to maintain competition.¹¹⁷

1. Possible Combinations

Given all of the speculation that there will be a major consolidation of the airline industry, how will the airlines be affected and who might the likely pairings involve? Numerous combinations have been mentioned in response to the growing merger speculation that has preoccupied the industry for the last few years. Potential buyers that have been mentioned include American Airlines, United Air Lines, and Delta.¹¹⁸ Potential sellers mentioned include USAir, Continental, Trans World Airlines, America West Airlines, and Alaska Airlines.¹¹⁹ It is speculated that Northwest Airlines could go either way.¹²⁰ Some possible combinations mentioned include American Airlines and Northwest teaming up and United and USAir forming an alliance.¹²¹ A mid-1997 analysis by NatWest Securities predicted

¹¹⁴ *Id.* (quoting Michael Boyd, an aviation industry consultant).

¹¹⁵ See Peltz, *supra* note 22.

¹¹⁶ *Id.* (quoting John Pincavage, an analyst with the investment firm of Dillion, Read & Co.); see also, *Top 1997 Issues*, *supra* note 37 (citing Phil Bageley, an analyst with Standard & Poor's on the possibility of only three or four major airlines).

¹¹⁷ See McCartney, *supra* note 41 (quoting Kevin Murphy of Morgan Stanley who points out that the air-express industry is fiercely competitive even though it is dominated by three players).

¹¹⁸ See *Top 1997 Issues*, *supra* note 37.

¹¹⁹ See *id.*

¹²⁰ See *id.*

¹²¹ See McCartney & Brannigan, *supra* note 38 (quoting Hollis Harris, a former Delta executive, former Continental director and retired chairman of Air Canada).

further industry consolidation via airline mergers with the probable catalyst being the AA-BA alliance.¹²² The NatWest analysts looked at two potential merger scenarios: (1) where no restrictions on capacity apply and (2) where capacity is restricted to thirty percent of the industry.¹²³ Each scenario was based on five criteria - fleet commonality, complimentary route systems, unit cost, culture, and pilot wage rate compatibility.¹²⁴ Based on these criteria, NatWest predicted the following combinations:

Scenario one: no restrictions on capacity

MERGER TEAMS	% of 1996 Capacity
United-Delta	38%
American-Northwest	32%
Continental-America West-Southwest-TWA	20%
Alaska-US Airways	9%

Scenario two: restricts capacity to 30% of the industry

MERGER TEAMS	% of 1996 Capacity
United-Southwest-Alaska	28%
American-Continental	27%
Delta-Northwest	29%
US Airways-TWA-America West	15% ¹²⁵

2. *Impact on Post-Consolidation Airlines*

The subsequent mergers formed after an AA-BA alliance could allow the remaining airlines to stay competitive (or at least afloat). However, there is always a toll taken on airlines that attempt to merge. As was discussed earlier in this Comment, most airline mergers in the past have been disasters.¹²⁶ Besides the financial hardships of merging airlines, there are a myriad of other factors to be considered. Different employees with different wage scales and work rules must be integrated.¹²⁷ In addition, computers, routes, airplanes, and maintenance must be meshed together.¹²⁸

¹²² See *Future*, *supra* note 61.

¹²³ See *id.*

¹²⁴ See *id.*

¹²⁵ See *id.*

¹²⁶ See *supra* notes 22-26 and accompanying text.

¹²⁷ See McCartney, *supra* note 41.

¹²⁸ See *id.*

A wave of airline mergers could effectively eliminate the smaller airlines from competition. Some analysts speculate that smaller, struggling airlines might not attract a larger, acquiring airline.¹²⁹ Given the power the new alliances would have, some of the smaller carriers might not be able to survive.¹³⁰ Thus, as larger airlines prepare for the problems associated with the post-consolidation industry, the smaller carriers may be in store for a fight for survival. Paul Tate, chief financial officer for smaller carrier Reno Air has stated that he “anticipate[s] a lot of pitched battles between large and small carriers. I expect there will be some very difficult wars for smaller carriers.”¹³¹ However, it might also be the case that the larger allied airlines may look to expand more of their international routes which could make room for smaller carriers to expand or merge domestically.¹³² So, there is the possibility that consolidation could mean that “the prospects for upstart carriers to find new niches [could] probably increase[].”¹³³

One positive effect that the AA-BA alliance could have for rival airlines is the opportunity to obtain some of the landing slots at Heathrow Airport that regulators have insisted be released before the alliance would be approved.¹³⁴ Therefore, at least internationally, the AA-BA alliance could open up some doors for carriers that have been excluded from Heathrow in the past. In addition, the combining of various airlines after the alliance could mean fewer airlines seeking slots and, providing an opportunity for more airlines to gain access to Heathrow.

B. EFFECT OF/ON AIRLINE EMPLOYEES

Consolidation in the airline industry likely to follow an AA-BA alliance would also have far-reaching effects on the employees of the airlines. However, the employees could prove to be a critical factor in determining the scope and success of post-alliance consolidation. This part explores the impact that airline employees could have on the wave of mergers that might follow the AA-BA

¹²⁹ See *Top 1997*, *supra* note 37.

¹³⁰ See *id.*

¹³¹ *Id.*

¹³² See *Delta-Continental May Not Fly*, STAR-TRIB. (Minneapolis-ST. Paul), Dec. 5, 1996, at 1D, available in 1996 WL 6939359 [hereinafter *May Not Fly*]. (citing Terry Trippler, editor and publisher of the newsletter *Airfare Report*).

¹³³ McCartney, *supra* note 41.

¹³⁴ See *Top 1997 Issues*, *supra* note 37.

alliance as well as the impact those mergers would have on them.

1. *Impact of Airline Employees on Consolidation*

One of the impediments to a successful wave of mergers following an AA-BA alliance would be the employees of the merging airlines. As was discussed earlier, one of the more difficult tasks facing merging airlines is how to integrate their employees. The problem has been stated succinctly:

Merging big airlines means melding tens of thousands of (often unionized) pilots, flight attendants, mechanics, reservation clerks and other workers who often have sharply different salaries, benefits and ways of doing their jobs.

It's a difficult, complex task that often disrupts employee morale and erodes the surviving airline's service and performance. Few airlines have accomplished it successfully.¹³⁵

Thus, airline employees can be the determining factor of an airline merger's success. Airline mergers in the past have been impaired by pilot union concerns about seniority rights.¹³⁶ For example, strong union opposition was identified as killing the proposed 1995 acquisition of USAir by United Airlines.¹³⁷ Potential mergers following the AA-BA alliance would face similar problems like those experienced in past acquisitions. While airline executives may have learned from past merger mistakes, the employees still have the same concerns and needs as in the past. As one analyst stated:

Yes, today's executives are different, but you're dealing with the same airline employees, the same unions and the same clashing cultures.

Integrating [two airlines'] labor forces is difficult, and that's why no airline merger has ever gone smoothly. . . . There's no reason to believe it can be done [now] any more smoothly than before.¹³⁸

Another reason to believe airline mergers could be hampered by employees is the fact that employees now carry more "clout" in the industry and are major stockholders in several carriers.¹³⁹

¹³⁵ Peltz, *supra* note 22.

¹³⁶ See *May Not Fly*, *supra* note 132.

¹³⁷ See *id.*

¹³⁸ Peltz, *supra* note 22 (quoting Raymond Neidl, an analyst with the investment firm of Furman Selz Inc.).

¹³⁹ See McCartney, *supra* note 41. For example, a 1994 employee buyout plan by United Air Lines allowed the pilots and machinists unions and salaried/man-

Therefore, airline employees may have more say in potential mergers than in the past. This could contribute to increased difficulties in effectuating successful mergers after an AA-BA alliance.

2. *Impact of Consolidation on Airline Employees*

Assuming airline consolidation is successful despite employee resistance, how will it affect airline employees? Airline employees no longer have the equity and employee welfare-based merger protection provisions they once enjoyed under the Civil Aeronautics Board.¹⁴⁰ Airline employees could face the problem that many entities have when they merge: how to integrate the personnel, cultures, and policies of two different organizations.

One particular group that could be affected by the mergers is airline unionized pilots. Unions use seniority rankings to determine which pilots fly the popular schedules and routes.¹⁴¹ Merging the pilot lists of two airlines could push pilots (as well as other employees) down the seniority ladder.¹⁴²

Another problem facing employees of post-merger airlines is the different cultures that now must be meshed together. In some instances, the two cultures never successfully merge, leaving airlines to "hold together factions as best they can like United Nations peacekeepers."¹⁴³ There is also the possibility that the merging of two airlines, like many mergers, could lead to a larger number of employees than jobs.

However, it should be kept in mind that all of the negative effects discussed here would be part of an effort by the airlines to stay competitive. The perception of the airlines may very well be that if they do not defend themselves via consolidation, they may not be able to stay competitive against the giant alliances that would form. Thus, if the airlines did not merge, their profits could decrease by such a margin that layoffs would happen

agement employees to acquire 55% of the company's shares. See *United Airlines: Flying the Friendly Skies of Employee Ownership* (visited Feb. 22, 1998) <<http://www.vais.net/~woa/articles/ual.htm>> (posting an abridged version of an article originally published in the Winter 1996 issue of *Working People*).

¹⁴⁰ See Gary S. Green, *Labor Protective Provisions in the Airline Industry*, C941 ALL-ABA 373, 377-94 (1994) (discussing the evolution of the CAB's protection).

¹⁴¹ See *May Not Fly*, *supra* note 132.

¹⁴² See *id.* (discussing the issue of pilot seniority in the context of the proposed Delta-Continental merger); see also Tomkins, *supra* note 30.

¹⁴³ McCartney, *supra* note 41.

anyway. Even worse (and more probable for smaller, struggling airlines), the new combinations that would result might force unmerged airlines into bankruptcy.

C. EFFECTS ON AIRLINE CONSUMERS

The possibility of airline consolidation could have far-reaching effects on airline consumers as well. There has been much speculation that a wave of mergers could cause airline fares to increase and service to decline. Many airline mergers in the past have resulted in higher prices, more restrictions, fewer flights and general problems in service for air travelers.¹⁴⁴ It has been argued that a wave of mergers could repeat these problems. However, others have suggested that mergers do not necessarily cause these problems and can actually benefit airline consumers.¹⁴⁵ The potential effects mergers might have on consumers can be broken into two main areas: price and service.

1. Price

Fares have generally risen as a result of past mergers where the new airline dominates the market.¹⁴⁶ For example, when Trans World Airlines (TWA) acquired Ozark Airlines in 1986, nonstop round-trip fares out of TWA's St. Louis hub rose twenty-three percent in two years.¹⁴⁷ The standard concern given when discussing airline mergers is whether or not it will affect competition. The reason behind this concern is that many believe mergers would mean less competition, causing higher fares.¹⁴⁸

If past individual merges have meant less competition and higher fares, it is very possible that a whole wave of mergers that could follow an AA-BA alliance would surely decrease competition and raise prices to some degree. In support of the proposition that decreased competition increases fares, consider a report released by the U.S. General Accounting Office.¹⁴⁹ It reported that travelers at big-hub airports dominated by a few carriers pay "substantially" higher fares than travelers who fly to or

¹⁴⁴ See Lisa Miller, *Airline Merger Offers Fliers No Pie in the Sky*, WALL ST. J. EUR., Dec. 6, 1996, at 8, available in 1996 WL-WSJE 10755555.

¹⁴⁵ See *id.*

¹⁴⁶ See *id.*

¹⁴⁷ See *id.* (citing a U.S. Department of Transportation investigation).

¹⁴⁸ See *id.*

¹⁴⁹ See Ed Perkins, *Mergers Will Squeeze Consumers*, ORANGE COUNTY REG. (Cal.) Feb. 9, 1997, at D04, available in 1997 WL 7406530.

from airports more competitive.¹⁵⁰ The report also concluded that larger airlines have erected barriers to effective competition at several of the nation's largest airports.¹⁵¹

However, others have argued that the merger of two large airlines does not necessarily mean that fares will increase.¹⁵² If one believes this position, it might follow that multiple mergers in an industry-wide consolidation would also not necessarily increase fares. One reason offered for this belief is the presence of low-fare carriers that were not as prevalent in the past.¹⁵³ Especially in the domestic context, the presence of low-fare competition could be the determining factor of whether newly merged airlines would increase their fares. As one commentator has stated, "[i]n the long run, [the presence of low-cost carriers] will be what determines air fares."¹⁵⁴ In addition, new "megacarriers" usually offer introductory bargains for weeks or even months.¹⁵⁵ For example, after TWA acquired Ozark, fares decreased in twenty-four of sixty-seven routes examined by the Department of Transportation.¹⁵⁶ Therefore, one could argue that fares may not increase after numerous mergers and could (at least temporarily) drop following industry consolidation.

Another potential benefit to consumers is frequent-flier miles. Consumers who participate in frequent-flier programs can receive benefits when airlines merge because the merged carriers usually have more destinations to offer passengers.¹⁵⁷ Thus, consolidation could potentially cause certain airline consumers to benefit the most from the mergers.

2. Service

In the past, airline mergers have caused increased problems in service to airline consumers. For example, a Department of

¹⁵⁰ *See id.*

¹⁵¹ *See id.* The article goes on to argue that if market concentration results in barriers to competition as the General Accounting Office report suggests, a merger between any two "megacarriers" would increase their ability to erect and maintain such barriers. *See id.* If one believes this line of reasoning, then multiple mergers involved with an industry consolidation would increase these barriers and almost assuredly increase fares.

¹⁵² *See id.*

¹⁵³ *See May Not Fly*, *supra* note 132 (quoting Terry Trippler, editor and publisher of the newsletter *Airfare Report*).

¹⁵⁴ *Id.*

¹⁵⁵ *See Miller*, *supra* note 144.

¹⁵⁶ *See id.*

¹⁵⁷ *See id.*

Transportation survey that analyzed consumer complaints about U.S. airlines attributed many of the problems to airline mergers.¹⁵⁸ When Texas Air Corp. consolidated People Express with two other carriers into Continental Airlines in 1987, consumer complaints rose dramatically.¹⁵⁹

Larger airline mergers have resulted in short-term impediments to service as the airlines try to work out problems with their schedules and operations.¹⁶⁰ Multiple mergers between numerous airlines could exacerbate these problems for consumers as several airlines could experience these problems simultaneously. If, as speculated in this Comment earlier, airline consolidation causes some smaller airlines to go out of business, this could also cause problems in service for airline consumers. It is possible that some routes would have less-frequent service if smaller coast-to-coast carriers disappear following consolidation.¹⁶¹

Consolidation could also cause increased layovers and mean new connecting flights for consumers, since merging airlines usually eliminate redundant hub operations.¹⁶² As one analyst has stated, "nonstop service is reduced when hubs are eliminated."¹⁶³

However, it is possible that multiple airline mergers could benefit airline service to consumers in the long run. Many newly merged airlines increase service in some cities.¹⁶⁴ Also, acquiring carriers could learn more efficient and popular service techniques from the airlines they acquire.¹⁶⁵ Thus, airline consumers who may not necessarily have a choice in which airline they choose (certain business travelers, for example) might benefit from new service techniques that an acquiring airline

¹⁵⁸ See *Complaints About U.S. Airlines Up Almost Seven-Fold In August*, J. RECORD (Okla. City), Sept. 5, 1987, available in 1987 WL 4325309.

¹⁵⁹ See Miller, *supra* note 144. The article quotes Mike Boyd of Aviation Systems Research Corp. as stating that "[t]here were literally riots' at airport gates." *Id.*

¹⁶⁰ See *id.* Illustrating this point, the article cites Steve Landes, head of the South Florida Commuters Association, who "recalls waiting hours for a flight in 1980 because Pan Am, after buying National Airlines, had trouble determining which plane to fly out of New York City." *Id.*

¹⁶¹ See McCartney, *supra* note 41.

¹⁶² See Miller, *supra* note 144.

¹⁶³ *Id.* (quoting Raymond E. Neidl, an analyst with Furman Selz).

¹⁶⁴ See *id.*

¹⁶⁵ See *id.* Speculating on the proposed Delta-Continental alliance, the article states that Delta (whose reputation among travelers had "faltered significantly" in past years) could learn something from the service provided by Continental (ranked as one of the most popular and efficient airlines in the country). See *id.*

might adopt following a merger with a more service-oriented carrier.

V. CONCLUSION

In the period of time between the initial research and the final editing of this Comment there have been no significant developments towards further implementation of the originally proposed American-British Airways alliance. Thus, the possibility of airline consolidation after this alliance remains only speculation. However, if the fully implemented AA-BA alliance is ultimately successful, it will most likely have far-reaching implications (possibly positive and negative) for all involved in the airline industry.

Airlines will feel the effect of the alliance as the balance of competition shifts (by the AA-BA alliance itself and the subsequent consolidation it will trigger). Airline employees will also feel ramifications through the problems faced by merging employees or the anxiety of employees of smaller airlines that might not survive in the post-consolidation landscape. Finally, airline consumers may face increased prices and diminished service or, perhaps, increased benefits.

Even if the AA-BA alliance ultimately does not come to fruition, the climate it and other proposed alliances have caused in the airline industry will surely continue to permeate the industry. Airlines will continue to prepare themselves for the possibility of teaming up with rival carriers to stay competitive after the alliance of two large airlines. Thus, any future talks between carriers will continue to fuel the current pro-consolidation sentiment of the airline industry.

**Tributes
to
Professor Walter W. Steele, Jr.**

